28 1975

IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

NO. 74-1651

RICHARD A. CLARK, JAMES H. EVANS, WESTON M. LENNOX, DAVID A. MOFFAT, SAMUEL L. SAVIDGE, GEORGE L. ZIMMERMAN and HELEN D. BLOOMFIELD,
Petitioners,

v.

H. R. WATCHIE and SHEILA WATCHIE, his wife, H. R. WATCHIE & ASSOCIATES, INC., a Washington corporation, E. JOSEPH McCAMBRIDGE and JANE DOE McCAMBRIDGE, his wife, GENE LYNN and JANE DOE LYNN, his wife,
Respondents.

BRIEF OF RESPONDENTS LYNN IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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Respondents.

BRIEF OF RESPONDENTS LYNN IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondents Lynn respectfully oppose the petition for issuance of a Writ of Certiorari to review a portion of the judgment and opinion of the United States Court of Appeals for the Ninth Circuit.

OPINIONS IN THE COURTS BELOW

Respondents accept petitioners' statement relating to the opinions below.

JURISDICTION OF THIS COURT

Respondents accept petitioners' statement relating to jurisdiction of this Court.

QUESTION PRESENTED FOR REVIEW

Did the District Court abuse its discretion in denying petitioners' motion that this case proceed as a class action?

RULES AND REGULATIONS INVOLVED

Respondents accept petitioners' statement relating to the rules and regulations involved.

STATEMENT OF THE CASE

Petitioners in 1961 each purchased one or more limited partnership units in a land syndicate named Cougar Mountain Associates. Respondents were associated with the entity that sold those units. Each unit cost Twenty Thousand Dollars. These purchases followed oral sales presentations made at different places and at different times by various salesmen and /or individuals associated with the management of the partnership. There was no written prospectus.

One of the petitioners, James H. Evans, was closely associated with Cougar Mountain Associates and its management, actually assisting in sales efforts. Another of the petitioners, Richard Clark, was an attorney. Another petitioner, Samuel L. Savidge, was the owner of an automobile dealership in Seattle. The background and investment sophistication of the other petitioners also varied. Other investors (the claimed "class") had similarly diverse backgrounds. They included numerous attorneys, stockbrokers, real estate salesmen, and sophisticated investors and businessmen.

Knowledge of the operations of the limited partnership also varied. Some of the investors had purchased units in other similar ventures organized by H. R. Watchie. Some

sold real property to this real-estate syndicate at prices now claimed to have been artificially set. Others were members of land syndicates that sold such property to the limited partnership. Some investors carefully researched the land and the syndicate operations before purchasing. Some relied largely upon H. R. Watchie's opinion in making their decision to purchase.

Pre-purchase communications differed substantially in individual cases. There were a number of meetings of prospective purchasers in which the general partner, H. R. Watchie, or an associate, would make an introductory oral presentation, followed by a question and answer session. Matters discussed at sales meetings would vary according to the knowledge, interests and questions of those involved. Petitioner Evans, for example, attended several of Watchie's sales meetings and testified he was able to learn new things on each occasion about the partnership. At the time he purchased his partnership interest, petitioner Evans was thoroughly knowledgeable about Watchie's operations.

These meetings would often be followed up with personal contacts by salesmen, who were themselves selected in part because of their diverse backgrounds and interests. In some cases there were no such contracts because of the close relationship between Watchie (or someone else involved in the sales) and the prospective purchaser.

The unit salesmen discussed the facts with purchasers and answered questions. Again, no single pattern dominated these sales contacts. Many of the prospective purchasers of units were well aware of the history of sales and resales of property at increasing prices in the general area. Many had intimate knowledge of H.R. Watchie's operation. Discus-

sions with potential purchasers would thus vary according to the information the individual already had.

In 1968, more than seven years after they bought units, the petitioners filed their complaint alleging fraud in the sale of securities. Respondents Lynn were not joined in the action until 1969. In their answers, respondents alleged that the statute of limitations had long since run on petitioners' claims. Petitioners responded that they had not learned of facts which would start the statute running until many years after their purchases. On a motion for summary judgment of dismissal, the court determined that a trial would be necessary to establish exactly when each purchaser had sufficient knowledge of the allegedly undisclosed facts to start the running of the statute of limitations.

The parties commenced discovery under the direction of a special master. Thousands of pages of depositions were taken, with much of the information relating to the class action issue.

Finally in January of 1971 the petitioners moved for a class action determination. But the motion was supported only by a five-page affidavit of petitioners' attorney and a memorandum containing largely conclusory statements about the appropriateness of class treatment. There were no references to the record to support the allegations. Respondents filed numerous affidavits, including those of several salesmen as well as that of H. R. Watchie. These affidavits, together with depositions and exhibits, demonstrated that representations varied significantly from purchaser to purchaser.

After thoroughly considering the affidavits, depositions, pleadings, motions and other papers, the special master

prepared a report containing findings and conclusions recommending against class treatment. Based upon its own review as well as the master's report, the district court found that the individual questions predominated over any common questions. The court therefore denied the motion for a class action.

The petitioners immediately filed a notice of appeal to the Ninth Circuit. Respondents did not object to petitioners taking an interlocutory appeal, but instead indicated that they felt it essential that the matter of class determination be finally resolved as early as possible in the proceedings so that uncertainty relative to the scope of discovery and relevancy of many facts could be avoided. The petitioners chose instead to voluntarily dismiss their appeal. All further proceedings, including discovery, were conducted on a non-class basis.

Thereafter, the district court granted respondents' motion for summary judgment on the basis of the collateral estoppel effect of a prior state court judgment relating to the same transactions. Petitioners appealed that decision to the Ninth Circuit, and at the same time sought review of the district court's decision denying class status. While limiting what plaintiffs could attempt to prove at trial, the court of appeals reversed the summary judgment on collateral estoppel, but affirmed the trial court's decision on this class action issue. Petitioners did not seek a rehearing or clarification by the court of appeals.

It is the Ninth Circuit's affirmance of the class action order that petitioners now seek to have reviewed by this Court.

ARGUMENT

1. The Class Action Determination by the Courts Below Raises No Issue Warranting this Court's Review

Petitioners do not take issue with the Ninth Circuit's recognition that a class-action determination is one of a trial court's considered discretion. Petitioners do not challenge the statement of the court of appeals that a trial judge's findings regarding the provisions of Rule 23 and their application to the case should be considered to be within his discretion.

Instead, petitioners in essence argue that the contentions which they made should have controlled the trial court's decision. In effect, petitioners' principal argument is that the trial judge's discretionary determination was wrong.

This argument simply raises an issue of fact which would require a detailed analysis of the record presented to the trial court. This Court pointed out in *United States v. Johnson*, 268 U.S. 220, 227 (1925): "We do not grant certiorari to review evidence and discuss specific facts."

Throughout this extended litigation, petitioners' class-action arguments have been based upon their contentions of facts rather than upon evidence of such facts. Even in their petition for certiorari, petitioners rely principally on what they "expect to prove" (pages A42-A57 of petitioners' appendix) and upon their "disputed contentions in the pre-trial order" (pages A57-A70 of petitioners' appendix). Of course, a party's contentions cannot, without more, serve as a basis for class treatment. Plaintiffs have the burden of proof with respect to each of the requirements of Rule 23. *Cf. e.g., DeMarco v. Edens*, 390 F.2d 836 (2d Cir. 1968); *Poindexter v. Teubert*, 462 F.2d 1096 (4th Cir. 1972).

Without the imposition of this burden a plaintiff would always gain class-action treatment simply by alleging the existence of common questions of law or fact.

When, as here, there is disagreement between the parties as to the facts, the trial court must consider the entire record as presented at the time the motion for class determination is made. Here the trial court had before it affidavits which flatly contradicted petitioners' unsupported contentions, demonstrating that there were few, if any, common questions and that individual questions predominated in the litigation. The special master and the district court judge also had before them thousands of pages of deposition transcripts as well as numerous other affidavits and papers relative to other aspects of the case, which would have to be considered in a review court. The trial judge was well aware of petitioners' contentions of nondisclosures and conspiracy.

The trial court correctly recognized that statements made or not made in connection with sale of the units would vary in the case of every sale. In addition, individual fact questions relative to the statute of limitations, estoppel and waiver, damages, and reliance upon affirmative representations,[1] also militated against class treatment. It

1. Petitioners state at pages 16-17 of their Petition that there would be an issue at the time of trial as to "which, if any, of the statements in the printed copies of the partnership articles were false?" Examination of the pre-trial order, however, shows that petitioners have not alleged that any of the statements in the partnership articles were false. If, despite the pre-trial order, petitioners were permitted to make such an allegation, this would raise at least two questions that would require individual analysis. The first would be whether or not each purchaser received prior to his purchase a printed copy of the partnership articles. According to his sworn testimony, petitioner Evans did not. The second question would be whether there was reliance upon any such positive misrepresentations by the petitioners or other purchasers in making their decision to purchase.

seems apparent that this Court should not direct its attention to the claim that the district court erred in analyzing the record. This issue, which would require review of factual determinations by the trial court in light of an extensive record, is not sufficiently important to warrant the Court's attention.

2. Rule 23 Clearly Requires a Finding That Common Questions Predominate. There is No Need for this Court to Issue an Opinion on that Portion of the Rule

Petitioners contend that the Ninth Circuit has added an additional requirement with respect to class action suits under Rule 10b-5 by requiring proof in this case that misrepresentations or non-disclosures were common to the class. Petitioners contend further that this raises an important question of federal law, requiring settlement by this Court. Neither contention has merit.

The ostensibly new class action requirement is, according to petitioners, contained in the language of the opinion quoted at the top of page 9 of the petition for certiorari. As quoted, the language reads:

> Appellants must show, as a condition to class status, that any misrepresentations or non-disclosures were common to the class. They have not shown that the alleged misrepresentations and nondisclosures involved every limited partner.

But the opinion is incompletely quoted. Without noting the deletions, petitioners have left out parts of the quoted sentences, and have also deleted reference to footnotes 13 and 14. The full paragraph, together with the explanatory footnotes, appears as part of the extract from the court's opinion on page A-1-2.

Moreover, when read in context with what precedes and follows the quoted language, it is apparent that the Ninth Circuit was responding to a specific argument of petitioners relating to the predomination requirement. The court simply recognized that even though petitioners might not have to establish reliance in this case (which would raise individual questions) there were still other impediments to class treatment, in particular the failure to show that all the limited partners were victims of the same alleged misrepresentations or nondisclosures. The trial court had found that common questions did not predominate. In the quoted langague, the court of appeals was discussing the trial court's finding and, in footnote 14, the court specifically referred to the predomination requirement by pointing out that appellants had the burden of proof on that issue.

This did not impose any "new" requirement with respect to class action suits. It has always been clear under Rule 23 that one party can represent all others in a purported class action only if that party can show first that in some respects at least his experience or claims are common to all. There is nothing new in such a requirement. The existence of common questions in any purported class action is a specific prerequisite to class treatment according to subsection (a)(2) of the rule.

But even a showing of common questions will not resolve the class issue, for under subsection (b) (3) of the rule there must be a finding that any such common questions of fact or law predominate over any questions affecting only individual members. The Ninth Circuit is thoroughly familiar with these requirements of Rule 23 and has applied them correctly. *See, e.g., Kline v. Coldwell Banker*

& *Co.*, 508 F.2d 226 (9th Cir.), *cert. denied*, No. 74-1196 (May 12, 1975); *In re Hotel Telephone Charges*, 500 F.2d 86 (9th Cir. 1974); *LaMar v. H.B. Novelty & Loan Co.*, 489 F.2d 461 (9th Cir. 1973).

The trial court in this case found that the sales presentations made by defendants were oral and the statements made or not made will vary in each case. The court therefore concluded that the required predominance of any common questions was absent in this case. The Ninth Circuit affirmed that ruling, recognizing that the trial court applied the proper rule of law and that its determination of class status is a proper exercise of its discretion.

There is no merit to the assertion that this application of the commonality requirement by the trial court, which was affirmed by the Ninth Circuit, threatens effective enforcement of the securities laws. The Ninth Circuit has been very protective of rights under Rule 10b-5, holding that in some circumstances, depending upon the relationship of the parties, mere negligence may be sufficient to justify imposition of liability under the rule. *White v. Abrams,* 495 F.2d 724 (9th Cir. 1974). When sales are accomplished through standardized means, such as through a written prospectus, then class-action status may be appropriate. But when, as here, there is little standardization, and any questions common to the purchasers do not predominate over individual questions, then remedies under the securities laws must be pursued on an individual basis.

3. There is No Conflict With the Decision of the Tenth Circuit in *Esplin v. Hirschi*

The Tenth Circuit, like the Ninth, will normally defer to the judgment of a district court in determining whether

a suit should be maintained as a class action. *Wilcox v. Commerce Bank of Kansas City,* 474 F.2d 336 (10th Cir. 1973).

At pages 12 through 13 of the petition, it is claimed that the decision of the Ninth Circuit conflicts with the Tenth Circuit's decision in *Esplin v. Hirschi*, 402 F.2d 94 *cert. denied*, 394 U.S. 928 (1968). Examination of the decision in *Esplin v. Hirschi* shows, however, that there were substantially different facts in the case. There the defendants admitted various nondisclosures. Certain omissions of material facts were "common to all purchasers." But more significantly, in addition to the 10b-5 claims *Esplin v. Hirschi* involved an alleged failure to comply with the Investment Company Act (a fact which is not even mentioned by the petitioners). The Tenth Circuit recognized that questions under that Act were identical as to each and every member of the class. Thus, the court stated, 402 F.2d at 99:

> Hence, while the propriety of allowing a class action on the 10b-5 count is an extremely close question, there is really little doubt, as to the Investment Company Act, that the common issues predominate. Consequently, there does exist as to the totality of issues a common nucleus of operative facts such as would justify allowing the class action to proceed under newly amended Rule 23.

There is no Investment Company Act claim in the instant case.

Because of these major differences in the facts and the legal issues involved, the Tenth Circuit's decision in *Esplin v. Hirschi* gives little guidance here. It certainly does not represent a conflict with the decision of the Ninth Circuit.

4. There is No Conflict in Principle With Decisions of the Second Circuit

There is no conflict in principle between the decisions of the Second and Ninth Circuits on the issues involved in this case.

The Second Circuit, like the Ninth and Tenth, normally defers to the judgment of a district court in determining whether a suit should be maintained as a class action. *City of New York v. International Pipe and Ceramics Corp.*, 410 F.2d 295 (2d Cir. 1968).

Furthermore, the Second Circuit, like the Ninth and Tenth, recognizes that the matter of communication between seller and purchaser may have great bearing on whether a class action is appropriate. The court in this case cited *Moscarelli v. Stamm*, 288 F. Supp. 453 (E.D.N.Y. 1968) and *Simon v. Merrill Lynch, Pierce, Fenner and Smith, Inc.*, 482 F.2d 880 (5th Cir. 1973) in pointing out that oral misrepresentations lead to individual questions because they are not standardized in the same sense as misrepresentations in a prospectus or financial statement. The Second Circuit recognized this same distinction in *Korn v. Franchard Corp.*, 456 F.2d 1206 (2d Cir. 1972). The court there observed that the pre-condition of commonality was satisfied by a prospectus which related to all investors. *Id.* at 1210. It went on to distinguish cases involving such common questions from *Morris v. Burchard*, 51 F.R.D. 530 (S.D.N.Y. 1971), pointing out at note 20 that *Morris v. Burchard* involved oral misstatements which were not standardized and which did not emanate from a single course of conduct.

Green v. Wolf Corp., 406 F.2d 291 (10th Cir. 1968), *cert. denied*, 395 U.S. 977 (1969), is also consistent with

the Ninth Circuit's ruling. The Second Circuit in that case agreed with the assertion that misstatements and omissions were present in all prospectuses, and the commonality requirement was thus satisfied. The Ninth Circuit discussed this exact point in footnote 13. As the court pointed out, a standardized prospectus could be assumed to have been received by all class members, thus justifying class treatment. The court observed, however, that a similar assumption could not be made on the facts of this case.

Petitioners cite *Competitive Associates, Inc. v. Laventhol, Krekstein, Howarth & Howarth*, C.C.H. Fed. Sec. L. Rep. ¶ 95,090 (2d Cir. 1975), as conflicting in principle with the decision by the Ninth Circuit. But that case did not involve a class-action question. The issue there was whether proof of direct reliance on false financial statements was necessary for recovery under Rule 10b-5. The Second Circuit rejected defendants' argument that because the case involved allegations of misrepresentation as opposed to non-disclosure the plaintiff had to show reliance in addition to causation in fact. Again, there is no conflict in principle with the Ninth Circuit's opinion. The circuit court in this case stated that although petitioners might not have to establish reliance in order to recover, this was not the essential issue relative to the class action.

CONCLUSION

This Court should deny the petition for a writ of certiorari.

Petitioners contend that there are two questions worthy of review. First, they ask whether there may "be a class action on behalf of all defrauded investors provided that the common issues predominate over the individual issues" although certain facts are not established to be identical

as to each investor. Certainly a class action may be allowed under such circumstances. Reference to the wording of Rule 23 makes it apparent that not *all* issues need be common to the class; rather, the requirement is that common issues must *predominate* over individual issues. Neither the Ninth Circuit nor the district court misperceived nor misapplied this rule. The district court found, on the basis of an extensive record, that common questions did not predominate over individual questions. Thus, it correctly found that the case was not appropriate for class treatment. The Ninth Circuit properly affirmed that decision.

Secondly, petitioners ask whether Rule 23 gives a district court the discretion to deny class status to a suit if there are common questions of law and fact that predominate over individual questions, merely because securities were sold with oral representations. Regardless of how that question is resolved, it is not relevant to this case. The question assumes that there are common questions of law and fact that predominate. Once again, however, that is not the situation in this lawsuit.

Despite their attempts to characterize the issues involved as important, novel, and unsettled in a manner demanding this Court's attention, petitioners' actual grievance is with the exercise of discretion by the trial court. That court properly exercised its discretion within the confines of Rule 23, and the Ninth Circuit affirmed that exercise after due consideration of whether or not the trial court had acted propertly. There is no need for this Court to review that decision.

Respectfully Submitted,

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APPENDIX

Portion of Ninth Circuit's opinion, *Clark v. Watchie*, 513 F.2d 994, 999-1000 (9th Cir. 1975):

The district court adopted the special master's report without extensive comment. The report stated that none of the Appellees made written representations to the purchasers of limited partnership units. The master reasoned that since the alleged omissions and misrepresentations were oral, separate determinations would have to be made of what was disclosed to each limited partner. He concluded that questions of law or fact common to the members of the class do not predominate over questions affecting only individual members.

Appellants contend that we should hold that common questions predominate. They reason that it is important that the presentations of some salesmen may have differed from others only if the element of reliance is a prerequisite to ultimate liability. In support of their contention that reliance is not an element in a 10b-5 suit, Appellants cite Affiliated Ute Citizens v. United States, 406 U.S. 128, 153-154, 92 S.Ct. 1456, 1472, 31 L.Ed.2d 741 (1972). There the Supreme Court said that "positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of the decision."

In so arguing, Appellants misconceive the issue. Although they might not have to establish reliance to ultimately succeed in the suit, Appellants must show, as a condition to class status, that any misrepresentations or non-disclosures were common to the class.[13] They have not done so for they have not shown that the alleged misrepresentations and non-disclosures involved every limited partner.[14]

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13. In this connection, the Second Circuit case, Herbst v. International Telephone and Telegraph Corp., 495 F.2d 1308 (2nd Cir. 1974), is inapposite. The Court held that since individual reliance was not an element, the district court did not err in holding that common issues of law and fact were predominant. In *Herbst*, the alleged misrepresentations were issued through a written prospectus. In certifying the suit as a class action, the district judge could have assumed that all class members received the standardized prospectus. A similar assumption cannot be made in this case. Furthermore, other courts have held that oral misrepresentations lead to individual questions because they are not standardized in the same sense as misrepresentations appearing in a prospectus or financial statement. See Moscarelli v. Stamm, 288 F.Supp. 453, 462 (E.D.N.Y. 1968); Simon v. Merrill Lynch, Pierce, Fenner and Smith, Inc., 482 F.2d 880, 882 (5th Cir. 1973).

14. Appellants have the burden of showing that common questions predominate. Cf. Poindexter v. Teubert, 462 F.2d 1097 (4th Cir. 1972).